

B. Program Overview.

As currently planned, the low income program will have four principal components: (1) bill assistance; (2) arrearage maintenance; (3) consumer education; and (4) public outreach. System customers eligible for the program will be able to participate in a bill payment assistance program to lower the household's monthly bills for sewer service. The goal of the bill payment assistance component is to help households offset the increasing costs of utility service by providing a credit for limited income customers. The billing assistance will be provided through a credit each billing cycle toward the customer's sewer account balance. The size of the credit will be based on several factors, including household size, household income, and amount of usage. The arrearage management component will help eligible customers maintain their sewer service by freezing past due balances and eliminating future finance charges in exchange for regular monthly payments under a three-year installment payment plan.

Upon enrollment, customers will also receive information regarding simple and affordable ways to save on their household water use. Because sewer bills in Jefferson County are principally volumetric, reduced water usage is the only way to directly reduce sewer bills. The customer education information will be mailed in the enrollment packet sent to the customer upon enrollment into the program.

A community outreach campaign will also be launched to provide information about the low income program through grassroots efforts by utilizing various channels that exist in the community. These channels will likely include enlisting the help of existing community based organizations in Jefferson County, working on opportunities for low or no-cost earned media, sewer bill inserts, and other low cost methods of communication. Efforts will also be made to leverage the program communications with those of the water, natural gas, and electric utility companies serving the County households.

C. Program Funding and Interim Implementation.

Most utilities in Alabama support their low-income assistance programs through donations from customers, usually through allowing customers to check a box on their bill authorizing a donation. Further, most of these programs are targeted only towards senior citizens with low-income levels. Many of the customers eligible for the utilities' low-income programs are also eligible to receive assistance from the federal LIHEAP program administered by the Department of Health and Human Services. Because ESD is not an energy provider, LIHEAP is not available to assist ratepayers in offsetting their bills from the System.

The Receiver's planned low-income program described above is aimed at a much broader class of ratepayers and is not intended to be age-restricted. In other words, the goal of this program is intended to reach all ratepayers with incomes below 150% of the poverty level who might need assistance in paying their wastewater bills. As a result of this broader eligibility, the Receiver's low-income program plan has different, and financially more significant, funding needs than similar programs at other utilities.

The Receiver faces significant obstacles in funding a program of this size and scope. The estimated annual funding needs for this program are in the range of \$2 million per year. It is

unrealistic to believe the System's customers (currently, approximately 144,000 customers) will make donations to the program sufficient to fully fund it.

Further, even though the program is intended to alleviate delinquent and uncollectable accounts, according to Alabama law, the program may not be funded by a diversion of system revenues as this would create a discriminatory rate system. "A discount rate to elderly, low-income, or fixed income patrons may violate constitutional or statutory prohibitions against discrimination in utility rates." 12 MCQUILLIN'S LAW OF MUNICIPAL CORPORATIONS § 34:195. Additionally, in an opinion upheld on appeal by the Alabama Supreme Court, the Alabama Public Service Commission has specifically found that low-income assistance programs funded by ratepayers are unjustly discriminatory, and that providing assistance to low-income households in meeting utility bills is the job of the state and local government, not utilities. *Greater Birmingham Unemployed Comm. v. Ala. Gas. Corp., et al.*, 86 P.U.R.4th 218 (Ala. PSC 1987), *aff'd on procedural grounds, Greater Birmingham Ministries v. Ala. Pub. Serv. Comm'n*, 539 So. 2d 187 (Ala. 1988).

The practical long term solution to funding the low-income plan, like almost all solutions in this matter, lies in a negotiated solution. If the debt were refinanced, it is possible that a low-income program could be fully funded with a long term or annuitized fund created with creditor contributions during that refinancing transaction. However, that prospect does not seem likely in the short term.

In the meantime, the Receiver will begin collecting donations from any and all available sources as soon as possible to begin the foundation of the low-income program. However, the best, and most logical, source of funding for the low-income program is monies the County has already received and that were specifically designated to assist in this regard. These monies would allow the low-income program to begin immediately assisting the System's low-income customers in significant and meaningful ways.

As part of its November 4, 2009 settlement with the SEC, JPMorgan paid \$50 million "to and for the benefit of [the County] for the purpose of assisting displaced County employees, residents, and sewer ratepayers."²¹⁶ In communications with the SEC, the County recognized that there was a "possibility" of an "increased burden on the sewer rate payers alone" and that "the County's sewer users include a disproportionate number of low income citizens who are ill-equipped to take on that burden." A copy of the County's letter to the SEC is included in the Appendix at A-24. JPMorgan made this payment to the County on November 9, 2009.

It is unclear what use the County made of the \$50 million it received from JPMorgan, but to date these monies have not been spent to assist displaced ratepayers.

It is entirely appropriate to utilize the JPMorgan proceeds to fund the low income program for a number of reasons. First, to the extent JPMorgan's actions harmed the County, that harm most directly manifested itself in costs that were directly attributable to and borne by

²¹⁶ Order Instituting Administrative Cease-and-Desist Proceedings, pursuant to § 8A of the Securities Act of 1933 and §§ 15(b) and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, *In the Matter of J.P. Morgan Securities Inc.*, SEC Administrative Proceeding File No. 3-13673 (Nov. 4, 2009) (emphasis added).

the System's ratepayers. Second, the citizens of the County who were most tangibly affected by this harm were the System's ratepayers who, as the County pointed out to the SEC, will have to pay higher sewer rates – now and in the future – as a result. Third, those citizens most directly impacted by the subject of the SEC settlement with JPMorgan are, as again pointed out by the County, those low-income ratepayers least equipped to take on the “burden” of higher rates that are necessary.

Shortly after being appointed, the Receiver reserved its right to make a claim on the \$50 million received by the County. A copy of the Receiver's letter is included in the Appendix at A-25. To the extent the County is unwilling to disburse this \$50 million to the Receiver for the purpose of assisting displaced ratepayers through the low-income plan, the Receiver reserves its right to seek additional relief from the Court in the Receivership Action or commence other litigation to compel the County to turn over the money to the Receiver. The County must assist the ratepayers in dealing with the “burden” it helped create. If the Receiver is unable to secure funding for the low income program through the \$50 million, it is likely that the program will not be implemented as planned at this time.

In addition, the County received an additional \$25 million pursuant to a Fair Fund distribution from the federal government in 2011. This \$25 million was paid to the government by JPMorgan as a result of the same SEC action. The Receiver reserves the right to also seek access to that \$25 million payment or some portion thereof.

VIII. Non-Rate Recommendations and Options for a Permanent Solution.

A. Explore Additional Revenue Sources Other Than Rates.

In addition to sewer user rates, there are other potential revenue sources or enhancements available to the County that would allow for greater balance in System finances. Revenue streams that are not directly tied to water usage also provide enhanced stability for System funding because they fluctuate less. If the County and/or the legislature were to implement some of these measures it would reduce the pressure to adequately fund the System solely through sewer user rates, and more equitably spread the costs of the System among all of the residents throughout Jefferson County that benefit from the public health service the System provides.

One source of additional revenue is an increase in the existing sewer ad valorem tax. As discussed in Section IV.B.2 *supra*, aside from an adjustment in 1978 to account for a change in property classification, the rate for the annual sewer ad valorem tax has not been increased since its establishment in 1901. As of 2003, the total tax burden within Jefferson County was well below the average for similar municipalities. Increasing the ad valorem tax would result in lower future sewer rate increases and would also more equitably spread the burden of paying for the System among all Jefferson County residents as the legislature originally intended, and the Alabama Supreme Court found in *Keene v. Jefferson County*, 33 So. 43 (Ala. 1903), is fair and justified.

An additional source of revenue is imposition of a clean water fee for all County residents or for residents not currently connected to the System.²¹⁷ While controversial, a clean

²¹⁷ Special Masters Report at 34.

water fee remains a viable and appropriate option to consider as a revenue stream. As the legislature and the courts have recognized, everyone in the County receives the public health benefits from the System's treatment of wastewater and protection of area water supplies. It is therefore not unreasonable to require everyone to contribute to ensure the System's continued viability.

A viable wastewater system ultimately serves to reduce the cost of water treatment by water providers. For instance, the progression of water treatment may be envisioned as a three rung ladder. The local water providers first take water from rivers and lakes. This is the middle stage of water quality ("Level B"). The water providers then clean the water up to a level that it is safe to drink ("Level A"). During the course of use, the water collects waste and drops to a level of very poor quality ("Level C") much lower than where it began naturally in rivers and lakes. Before the System can discharge the poor Level C wastewater back into our waterways, it must treat the water and bring it back up to a level of quality slightly above Level B.

Treating water costs money. If the quality of water discharged into waterways by the System were lowered (less than Level B), the water providers would have a longer way to go, and would have to spend more money, in order to clean the water back up to a level safe for drinking (Level A). This cost would be passed on to everyone who uses the water works systems. Besides running afoul of numerous clean water requirements, this would spoil our waterways such that no one could swim or fish in them, as happened in this County in the mid-1950s and led to the lawsuits which resulted in the Consent Decree.²¹⁸ Moreover, a deterioration of water treatment in this County would likely lead to an overall decline in the overall condition of water in the County and diminish the quality of life, property values, and prospects for economic development for all of the County's residents.

An obviously better approach is to make sure the water is treated to an acceptable level before it is discharged into the waterways, as the System does now. This shifts some of the cost of treatment from the water provider to the System, but the beneficiaries remain the same – all citizens of the County. This benefit, among others, makes it reasonable for all citizens of the County to participate at some level in funding the System.

A clean water fee is legal because Alabama governments have the authority under their police powers to generate sufficient revenues from their residents in order to operate sewer systems.²¹⁹ The Alabama Supreme Court recognizes that the "beneficial effects" of this very System "extend to the entire county" and that "[t]he health of the valleys drained is of great importance to every citizen of the county."²²⁰ Therefore, fees levied on beneficiaries of the System are legal and help to spread the cost of the System over a wider tax base, thus reducing the average individual burden.

The System was created to protect the quality of "any and all streams and water courses" within Jefferson County, and it is this purpose that the System still serves today.²²¹ In 1953, the

²¹⁸ See, *supra*, Section II.B.3.

²¹⁹ See, e.g., *Bd. of Water & Sewer Comm'rs of the City of Mobile v. Yarbrough*, 662 So. 2d 251, 254 (Ala. 1995).

²²⁰ *Keene*, 33 So. at 438.

²²¹ Act 714, passed in 1901, gave the new Sanitary Commission (now the County Commission) the "duty to protect from pollution any and all streams and water courses from which any municipality or community draws or uses in

County Board of Health issued a warning to *all* County residents not to fish or swim in any open stream in Jefferson County because “*all watersheds in this area* carry pollution from sewage.”²²² Clearly, if all residents were being harmed by the pollution, all residents of Jefferson County benefit from the clean water the System protects, and all county residents, not just System customers, should contribute to the costs of providing this important public service.

B. Ensure that the System Has the Clear Authority to Enforce Mandatory Hookup to the System.

The System must have the authority to enforce mandatory hookups for new development, and for existing homes and businesses that can be served by the current System. This authority is commonplace for sewer systems across the country. *See, e.g.*, 56 AM. JUR. 2D *Municipal Corporations* § 504 (“A municipality may require that owners of premises served by a public drain or sewer connect to it, in the valid exercise of its police power.”); 64 C.J.S. *Municipal Corporations* § 1537 (“In the interest of the public health and welfare, a municipality may require property owners to connect with a sewer at their own expense”). Mandatory sewer connection requirements have also been routinely upheld as valid by the courts. *See, e.g.*, *Keys Citizens for Responsible Gov’t, Inc. v. Fla. Keys Aqueduct Auth.*, 795 So. 2d 940 (Fla. 2001); *Wolfe v. City of D’Iberville*, 799 So. 2d 142 (Miss. Ct. App. 2001); *Caddo Parish Sewerage Dist. No. 7 v. Reeves*, 649 So. 2d 1236 (La. Ct. App. 1995); *Loggins v. Lightner*, 897 S.W.2d 698 (Tenn. Ct. App. 1994); *Lepre v. D’Iberville Water & Sewer Dist.*, 376 So. 2d 191 (Miss. 1979). The United States Supreme Court has stated, in a case arising out of Georgia, that:

It is the commonest exercise of the police power of a state or city to provide for a system of sewers, and to compel property owners to connect therewith. And this duty may be enforced by criminal penalties.

Hutchinson v. City of Valdosta, 227 U.S. 303, 307 (1913).

Numerous municipalities in Alabama have passed ordinances requiring mandatory connection to sewer systems. *See, e.g.*, Prattville, § 66-80; Mobile, § 701.2; Guntersville, § 12-33; Ozark, § 10-72; Madison, § 13-60; Opelika, § 28-81(d); Wetumpka, § 82-73.

Alabama courts have also long recognized that the authority to enforce mandatory hookup requirements is vital to the establishment of an efficient sewer system:

[S]urely no sewerage system could be regarded as efficient without the incident of power in the municipal corporation to compel connections of property by its owners with the system.

Allman v. City of Mobile, 50 So. 238, 241 (Ala. 1909); *see also City of Leeds v. Avram*, 14 So. 2d 728, 729 (Ala. 1943) (recognizing that the burden of requiring a property owner to connect to the sewer system “offends no constitutional right”); *Town of Leeds v. Cason*, 116 So. 519, 519 (Ala. 1928).

whole or in part its supply of water.” *See* discussion in Section II.B.1 *supra*.

²²² *See* discussion in Section II.B.3 and PARCA Report at 43.

The County's lack of clear legal authority to enforce mandatory connection to its sewer system has been repeatedly recognized throughout the System's history as a near insurmountable barrier to the establishment of an efficient county-wide sanitary sewer system in Jefferson County.²²³ The problem has been identified, and the solution is obvious. Requiring mandatory hookups to the sewer System where available, will increase the number of ratepayers, and thus spread the costs of the sewer system more equitably among those who benefit from it.

Until hookup becomes mandatory, a reserve capacity charge could be implemented for County residents who are not currently connected to the System but could be.²²⁴

C. An Independent Public Corporation Should Be Created to Take Over Operation and Maintenance of the Jefferson County Sewer System.

As discussed previously in Section III.C, the Receiver has worked to facilitate and support the necessary legislation to create an Independent Public Corporation ("IPC") that would ultimately hold the System's assets, operate the System, and be obligated to pay the refinanced debt. The County has developed draft legislation for the IPC but it has not been presented to the legislature. This legislation is critical to the System's long term success and financial viability.

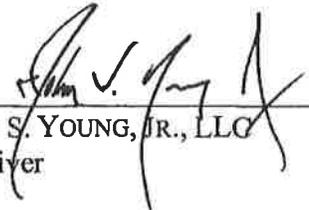
The IPC would have an independent professional board and strict governance documents to ensure the proper operation and funding of the System. The establishment of an independent professional board insulates the System from the influence of state and local political gamesmanship that throughout the System's history has prevented the establishment of a viable, professionally run, adequately funded System with the assets and resources necessary to serve the public. The governance documents will implement strict regulatory and operational controls that will prevent the manipulation, risk-taking, and corruption that occurred following the 1996 Consent Decree from ever happening again. The establishment of an IPC, with the requisite governing and regulatory controls, is the only hope the System has of being able to go to the market and attract future investors.

IX. Conclusion.

This concludes the Receiver's First Interim Report on Finances, Operations, and Rates of the Jefferson County Sewer System. The Receiver intends to submit its next interim report within the next six to twelve months. As noted earlier, the Receiver encourages the County, its various creditors groups, and all stakeholders to continue pursuing the negotiated solution that is critical to the long term financial health and viability of the System and the County, and the Receiver remains available to assist the parties in these negotiations in any manner they deem helpful. In the meantime, however, the Receiver will continue to move forward with the operations and capital plans to achieve efficiencies and best practices to preserve the reliability and compliance of the System. The Receiver will also continue to implement multiple future rate increases every six to twelve months until System revenues reach a level sufficient to support the System's operations and meet its obligations.

²²³ See Section II.B *supra*.

²²⁴ Special Masters Report at 29-30.



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Certificate of Service

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